

Chapter Two: Revenues and Rebates

A Review of Income Stream and Reimbursement from Montgomery County for Duplicative Services

Background

The City of Takoma Park in FY05 received rebates for police, road maintenance, crossing guards and park maintenance, totaling \$3.1 million.

Table 1. FY05 Montgomery County Rebates to Takoma Park

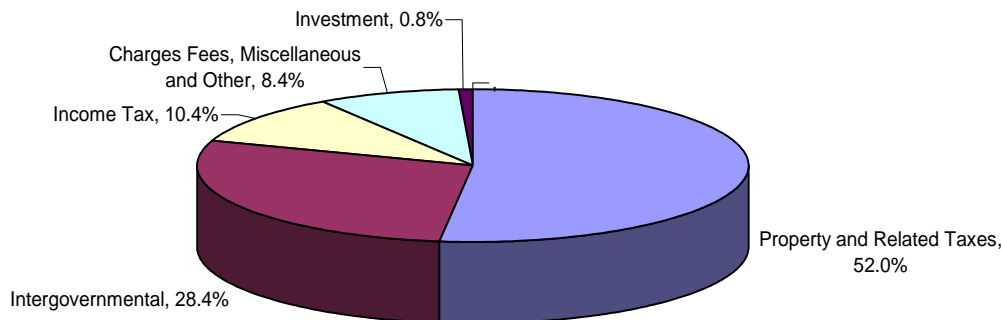
ACTIVITY	AMOUNT	% OF TOTAL REBATES
Police/MOU	\$ 2,061,318	68 percent
Police/County Code	\$ 495,585	15 percent
Road Maintenance	\$ 339,903	11 percent
Crossing Guard	\$ 121,738	4 percent
Parks	\$ 71,740	2 percent
TOTAL	\$ 3,090,284	100 percent

The police services rebate -- \$2.5 million -- represented the largest portion of the County's reimbursement for duplicative services. In addition, the City received payments from Montgomery County for Takoma Park expenditures associated with the Takoma Park Library and its maintenance of the Takoma Park Recreation Center on New Hampshire Avenue. These are not technically considered "rebates" under County law.

In FY 2005, the total budget for the City of Takoma Park was \$15,383,186 of which \$3.1 million, or about 19 percent of all revenues, was received as rebates for duplicative services from the County.

City Revenue Analysis

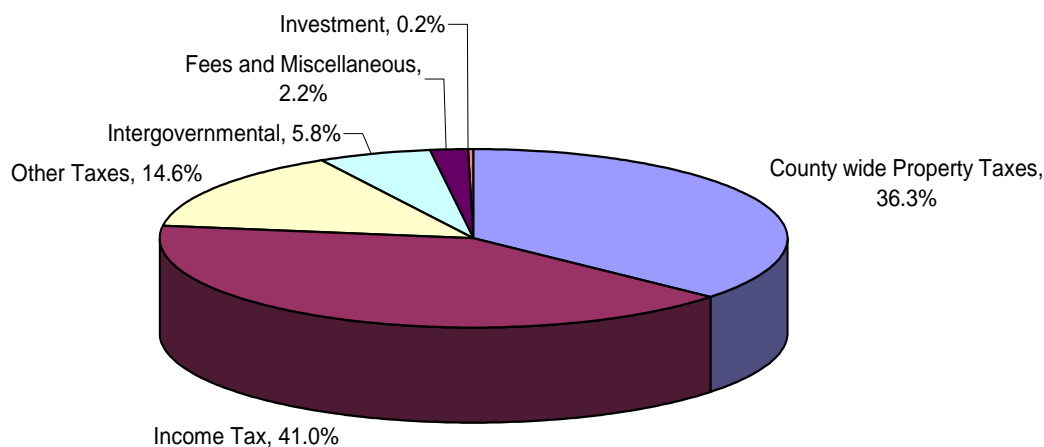
The City depends on property taxes to provide \$6.8 million, or about half of the City's \$14.2 million in general fund revenues: \$14.2 million. The next largest source, representing a little more than a quarter of all revenues, is intergovernmental funds, which come from other levels of government. The vast majority of this source is the County rebates. The City also receives a small share of the local income tax that City residents' pay, which represents about 10 percent of city revenues. (The local income tax is discussed in greater detail below). Fees, fines, licenses, permits, investments and other miscellaneous income make up the balance of City revenues. The Chart on the next page shows the major revenue sources. Details on the breakdown can be found in the Appendix.

Figure 1. FY05 Takoma Park General Fund Revenue Sources

Note: Chart does not include Appropriated Surplus, which makes up 7.6 percent of the General Fund.

County Revenue Analysis

The County's top revenue source is the local income tax. Property taxes are a close second. Together these two revenue sources make up more than three-fourths of the County's \$2.2 billion in general fund revenues. Most of the remaining revenues are from "other taxes," which include energy, telephone, and real property transfer and recordation taxes. Intergovernmental funds make up a small portion of the County's general fund. Service charges, fees and other miscellaneous sources also represent a small portion. Details on county revenues can be found in Appendix A and Table 14.

Figure 2. FY05 Montgomery County General Fund Revenues

What City Residents Pay in County Taxes – And What They Get Back

Takoma Park residents pay an estimated \$21.1 million in taxes to Montgomery County, primarily through property taxes and local income taxes but also including “other” special taxes. After rebates and other payments, the net payment from city residents to the County is \$17.8 million. By comparison, the City collects \$8.3 million from city residents, less than half of what the County takes.

Details on the various taxes the County collects from city residents are shown in Table 2 below.

Table 2. Summary of FY05 Revenues Received by Montgomery County from Takoma Park Residents

Source	Revenues (in millions)	\$ Paid Per Average Household	Comments
County-wide Property Tax Payments	7.6	1,103	0.734 tax rate
County Special Area Property Tax	2.8	406	0.272 tax rate
Total for all County Property Taxes	10.4	1,509	
Income Tax	8.7	1,262	3.2% tax rate
Pass back from County	(1.5)	(218)	17% returned to City
Net Income Tax	7.2	1,045	Retained by the County
Other Taxes	3.2	464	estimated
Base Solid Waste Management Fee	0.3	44	estimated
Total Revenues	21.1	3,061	
Less Rebates and Other Payments	(3.3)	(479)	
Total County Revenues from Takoma Park	17.8	2,582	

The County-wide real property tax rate is \$0.734 per \$100 assessed value. Based on a net assessable property tax base of nearly \$1 billion in Takoma Park, this amounts to about \$7.6 million that is raised through property taxes in Takoma Park. The county also charges Takoma Park residents a “special area tax” that adds another \$0.272 to their county tax bill for a combined property tax rate of \$1.006 per \$100 of assessed value. **This amounts to total property tax payments of \$10.4 million from Takoma Park.** The special area taxes are dedicated to mass transit, fire protection, recreation facilities and programs, and the Maryland National Capital Park and Planning Commission.

In Maryland local taxes are collected by the State through what’s referred to as a “piggyback” tax. It has acquired this name because, although the County sets its local tax rate, the tax is acquired through the state’s collection of income taxes. The state then distributes the local tax back to the counties and localities. Montgomery County sets the income tax on taxable income at 3.2 percent. **In the approved FY 2005 City budget, the amount of local income taxes passed back to the City amounts to \$1,481,000.** This represents 17 percent of the income taxes that Takoma Park taxpayers pay

to Montgomery County. The 17 percent share is set by state law.¹ Calculating backward, by dividing \$1,481,000 by 17 percent, the Takoma Park income tax contributions totals \$8.7 million. **After the 17 percent pass back, the net contribution to the County from Takoma Park is \$7.2 million**, or about \$1,000 for the average Takoma Park household.

Takoma Park residents also pay additional amounts in “other taxes,” such as the energy tax, the telephone tax, as well as real property transfer taxes and recordation taxes whenever they buy sell or refinance their property. The total amount that city residents pay in “other” taxes is not readily known. It depends on how much and what types of energy city residents buy, their telephone usage patterns, and how often they buy, sell, or refinance their real property. If Takoma Park contributions equal their share of the total county assessable tax base, then city residents contribute an additional \$3.2 million in “other” taxes, equivalent to about \$464 per household.

In addition, city residents pay the County a solid waste management base fee of \$39.69 per household, a total of roughly \$300,000 based on figures from the City’s storm water management program.

Incidence of Property Taxes and Fees of Takoma Park Residents

The Committee investigated the property tax burdens of Takoma Park residents to determine how significant the property tax burden is on various types of residents. We found that because of a property tax credit Takoma Park gives to low-income homeowners, the City’s tax burden is more progressive than in Rockville, Hyattsville, and unincorporated Silver Spring. A low income Takoma Park homeowner in a \$150,000 home pays approximately \$600 less in property taxes than that same household in Silver Spring. The tax burden is about the same as the other jurisdictions for a retired couple, and a median income household in a \$150,000 home. It is also about the same for a low-income household in a \$300,000 home. However, for all households in homes valued at \$500,000 or more, the Takoma Park tax burden is considerably higher than in the other jurisdictions. This higher tax burden, however, is mitigated by the fact that Takoma Park residents pay less in fees, and are able to deduct a greater portion of their local tax burden from their State and Federal income taxes. A detailed description of this analysis can be found in Appendix E.

Findings

Based on our analyses of tax and revenue issues, the Committee has arrived at the following findings.

Local Income Tax Pass Back Is Not Adequate

As described above, state law provides for a local income tax pass back of 17 percent of the local income tax revenues derived from a municipality. Consequently, the City gets \$1.5 million of its \$8.7

¹ See Annotated Code of Maryland Article Tax General § 2-607.

million in local income tax contributions passed back. This represents about 10 percent of the City's general fund revenues. However, the local income tax is the largest source of County revenues representing 41 percent of its general fund revenues. This disparity seems to indicate that income taxes, which are a progressive and flexible source of revenues, are not being shared in appropriate proportion with the City.

Inquiries into the origin and rationale for the 17 percent pass back yield little insight into its adequacy or fairness. The 17 percent level was set arbitrarily and irrespective of the level of services a city provided or the city's capacity to raise additional revenues. Consequently the 17 percent pass back should be seen as a floor for what should be shared with the city rather than as a fixed level for all cities.

To be fair the local income tax pass back should take into account the level of services that a city provides and correct for inequities in a city's capacity to raise additional revenues. For cities that provide more services and contribute more to the quality of life of residents in and near the city, it makes sense for the county to give back a larger share of the income derived from that city's residents.

The failure to account for a city's fiscal capacity is a major problem that undermines cities' ability to address the needs of residents who would have greater needs. This is because cities with less affluent residents are more likely to need more and higher quality services, but under the current system a small affluent city will get disproportionately more income tax revenue per person than a less affluent city. This reinforces current inequities keeping fiscal resources away from cities serving residents with greater needs and keeping fiscal resources in affluent communities.

The inequity of the current formula is evident in the contrast between the local income tax returned to Takoma Park and Chevy Chase Village. According to the 2000 Census, Chevy Chase Village has a population of 2,043 and a median household income in excess of \$200,000. In FY 2005 it received \$1.2 million from the income tax pass back, which represents almost half of its total revenues. The pass back to Chevy Chase equals about \$592 per person. In contrast Takoma Park, which has a population of 17,299 and a median household income of \$48,490, received \$1.5 million or only \$85 per person. The poverty rate in Takoma Park is over 10 percent, but only two percent in Chevy Chase Village. The current formula is not adequate for cities, like Takoma Park, that serve a relatively large number of lower income residents.

One way to make the income tax pass back more fair would be to create a formula that is tied to the level of services that a city provides and that does not unfairly penalize or reward a city for its residents' level of income. The best way to do this may be to use the city property tax rate relative to the county rate to determine the portion of income taxes passed back. The property tax rate is a reasonable proxy measuring the level of services a city provides. Cities with high tax rates also provide high levels of services. The city property tax rate also takes into account the city's fiscal capacity. Affluent cities can raise more money with lower tax rates than less affluent cities because their per capita tax base is larger. Less affluent cities, however, need higher tax rates to raise as much money. In effect, the income tax pass-back would offer matching funds to a city's own efforts to raise revenues for funding services.

If in Montgomery County the income tax pass-back was based on a city's property tax rate relative to the county rate with a 17 percent floor, Takoma Park, Rockville, Gaithersburg, and five other municipalities would be able to keep a greater portion of their income tax contributions. The change

would have no effect on the other municipalities. Under this formula, the City would get back about \$197 in income taxes per person, instead of \$85 per person.

In the recent state legislative session a bill, SB 724, was introduced that would reconsider municipalities' share of the local income tax. Although this legislation was not enacted, the fact it was considered affords an opportunity to discuss this issue with state and county officials.

Regional Revenue Sharing

In other metropolitan regions of the country, providing fiscal resources to communities with greater needs is often done through regional revenue sharing. For example, among seven counties in the Twin Cities metro area in Minnesota, each community contributes 40 percent of the growth of its commercial and industrial property tax base to a regional pool. The funds are then redistributed based on a formula that takes into account a jurisdiction's population and fiscal capacity, defined as per capita real property valuation. This program is credited with reducing tax-based disparities among Twin Cities communities from 50:1 to roughly 12:1. Regional tax sharing has also been implemented in the Hackensack Meadowlands region and is currently being considered in Sacramento, California. This is an important option to be considered for Montgomery County and the Washington D.C. metropolitan area. Further discussion of this option can be found in Appendix F.

There is Precedent for Keeping Some County Revenues in the City

The Committee has estimated that Takoma Park residents pay an additional \$3.2 million in taxes for energy, telephones, and real property transactions. All of these go into the County's general fund. It is entirely appropriate for city residents to make these payments, but for some of these revenues it may be reasonably argued that a portion of the revenues should stay with the municipality. There is precedent for this with other taxes. For example, the County Hotel Motel tax is shared evenly with the City for the one motel in Takoma Park, the Takoma Park Quality Inn and Econo Lodge. County law also allows the City to retain any taxes on admissions to movies, concerts, and other commercial entertainment ticket sales for events in Takoma Park. Similarly, it might be argued that for properties located in Takoma Park some portion of the real property transfer tax and the recordation tax be shared with the City.

Options for Enhancing City Revenues

There are a number of options for the City to enhance its own revenues, other than by increasing property tax revenue. The options readily available provide small amounts of revenue, and generally impose some costs or diminish services in some way. In recent budget discussions City staff provided a list of potential budget cuts that included some revenue enhancements. Some of these have been enacted and have or will shortly go into effect.

There are three major areas where significant revenue enhancements are possible:

Institute Payments in Lieu of Taxes (PILOTs)

Nonprofit organizations are exempt from paying taxes. This means that buildings owned by churches, nonprofit education institutions, and nonprofit service organizations, including hospitals, are all exempt from paying real property taxes on the land and buildings they own in Takoma Park. In many jurisdictions throughout the country large nonprofit institutions have made agreements with local governments to make a contribution to the local recognition of the services that local governments provide. In Takoma Park two large institutions -- Washington Adventist Hospital and Columbia Union College -- may be in a position to make such contributions. These institutions are very large and the possibility exists that PILOTs may be significant.

Takoma Park currently receives PILOT revenue for an affordable housing project, Edinburgh House, but not for the major nonprofit institutions. The PILOT for Edinburgh House expires with this fiscal year. The major obstacle to developing this potential revenue source is that no nonprofit institutions in Montgomery County pay PILOTs and there is no model or guidelines for negotiating and implementing it.

PILOTs are generally negotiated with nonprofit institutions, but Takoma Park also provides services to such county institutions as Montgomery College and the public schools. This raises the possibility of negotiating some payment for the services that the City provides to county institutions located inside Takoma Park.

Increase Fees, Permits, Licenses, and Fines

At the suggestion of City staff, the City Council recently enacted increases in certain service charges, fines, and fees for permits and licenses.

Table 3 shows a list of items in the budget that provide revenue through service charges, licensing, and permits with the revenue raised in the FY 2005 approved budget. One option related to fees is to have the City staff regularly assess city services and suggest changes in fees and fines where it may be appropriate.

Table 3. Revenues from Takoma Park Service Charges

Category	Service	FY 2005 Revenue	Comments
Service Charges	Protective Inspection & Rental Licenses	28,500	Multifamily Dwellings was \$68 in FY 2000
Service Charges	Commercial Inspections	40,000	\$75 & \$225 per business depending on sq. ft. of space
Service Charges	Public Parking Facilities	54,000	Parking meters
Service Charges	Waste Collection and Disposal	85,000	Public Works from Multi-family Housing
Service Charges	Classes	32,000	Recreation Dept.
Service Charges	Sports	14,000	Recreation Dept.
Service Charges	Youth Outreach	3,000	Recreation Dept.
Service Charges	Special Programs	10,000	Recreation Dept.
Service Charges	Summer Camp	35,000	Recreation Dept.
Service Charges	After School Program	50,000	Recreation Dept.
Service Charges	Facility Rental	5,000	Hefner and Municipal Building
Service Charges	Library Fines	20,000	
Service Charges	Takoma Langley Contractual Services	18,000	Takoma Langley – revenues from classes by outside contractors
Service Charges	TL Recreational Membership	5,000	TL – Rec. Center, gym & weight room
Service Charges	TL Facility Rental	8,000	Takoma Langley
Service Charges	TL Programs	19,000	Takoma Langley
Service Charges	Donations	5,000	
	Total Service Charges	621,500	
Miscellaneous	Copying	3,000	
Miscellaneous	Advertising – Bus Shelters	4,000	
Miscellaneous	Farmers Market	3,500	
Miscellaneous	Telephone Commissions	1,000	For pay phones
Miscellaneous	Recyclable Sales	1,000	Public Works
Miscellaneous	Mulch Sales	12,000	Public Works
Miscellaneous	Passport Service	30,000	
Miscellaneous	Special Trash Pickup	8000	Public Works
	Total Miscellaneous	62,500	
	Grand Total	684,000	

Source: Takoma Park Approved FY 2005 Budget and City Revenue Handbook

Monitor the City Share of Intergovernmental Grants

The County's fiscal year 2005 budget includes \$73.3 million in grant revenue, primarily from state and federal sources, for well over 150 programs. The grants range in scope from affordable housing to alcohol and drug abuse prevention, to refugee assistance. Many of these grants not only provide projects and services to County residents, they help fund the County government by allowing for administrative costs.

An overwhelming majority of the grants that the County receives are not "passed through" to, nor duplicated by, the City of Takoma Park. The primary question we should be asking regarding these non-pass-through/non-duplicated funds is whether Takoma Park residents are receiving their fair share of the benefits these grants provide. Fair share might be determined by estimating Takoma Park's portion of the County's eligible resident population. A limited analysis (perhaps looking at just a few of the larger grants) might help us gauge Takoma Park residents' relative participation in countywide programs.

The County passes through some funds from a very limited number of programs to Takoma Park. The FY 2005 Takoma Park budget includes \$179,525 in CDBG funds from the county's federally mandated allocation of \$4.3 million. This represents an adequate "fair share" amount since it approximates the City's portion of Montgomery County families in poverty. Other than the Community Development Block Grant (CDBG), however, the city's access to these funds is inconsistent from year to year.

The City could analyze the County's distribution of state and federal grant funds in order to determine whether residents of Takoma Park are receiving their "fair share". It is important to keep in mind that Takoma Park residents not only provide the County with revenue directly from tax collections, but also from revenues based on its total population and estimates of resident and community needs. The City's share of the benefits provided by those revenues should be proportionate to its share of the County's needs.

Summary of Recommendations

Based on the findings and analysis above, the Committee offers the following options for enhancing Takoma Park revenues.

- The City should negotiate more accurate rebates for services duplicated by the County and City;
- The City should advocate reform of the County's income tax pass-back by calculating the pass-back based on the City's property tax rate relative to the County's property tax rate, or by increasing the 17 percent floor;
- The City should initiate discussions of regional revenue sharing with county and state officials, as well as with regional government entities such as the Metropolitan Washington Council of Governments;
- The City should extend revenue sharing agreements to the County's "other taxes" derived from Takoma Park, such as extending the 50/50 share of the hotel/motel tax to bed and breakfasts, and retaining some portion of real property transfer taxes and recordation taxes;
- The City should seek to institute a system of payments in lieu of taxes from major Takoma Park nonprofits, such as Washington Adventist Hospital;
- The City should negotiate payments from the County for services provided to county institutions inside city limits, such as Montgomery College and the public schools;
- The City should regularly assess city services to determine where service charges, fines, and fees for permits and licenses might be increased; and
- The City should monitor intergovernmental grants to ensure that Takoma Park gets a fair share of the grants based on city need.